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Sharing Responsibility in Building the Future: A Business Perspective.

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The last occasion on which I spoke to the Social Justice Ireland Annual Social Policy Conference was in June 2008. I was asked to address the theme ‘*Making Choices: Securing Futures – Ireland at a crossroads*’. Three months later Lehman Brothers collapsed and the world changed. Little did we know that were not so much at a crossroads as on the edge of an abyss.

The ensuing three years have shaped the narrative around today’s conference. The capitalist system has been under siege. Business has been viewed as a major cause of social, environmental and economic problems. The Council of Europe’s draft charter on shared social responsibilities, the text of which appears at the beginning of this publication, urges companies:

‘to take account, in their strategies, of the interests of all stakeholders, both internal and external, and of the impact of their activity on society at large, going beyond a reductive view of economic efficiency that ignores collective well-being and drawing inspiration from the principles of the socially responsible and solidarity-based economy’.

While I agree with the thrust of this sentiment, I can’t help feeling that it is derived from a paradigm that pits business and society against each other. This is in part because economists have added legitimacy to the idea that to provide societal benefits, companies must temper their economic success. In neoclassical thinking, a requirement for social improvement – such as improved working conditions or hiring people with disabilities – imposes a constraint on the company. According to this theory, adding a constraint to a firm will inevitably raise costs and reduce these profits.

A related concept is the notion of externalities. Externalities arise when firms create social costs that they do not have to bear, such as pollution. Therefore, society must impose taxes, regulations and penalties so that companies ‘internalise’ these externalities. This belief still influences many EU and government policy decisions.

In fairness, the draft Charter urges companies to ‘seek lasting competitive advantages by taking into account societal values and social and ecological needs.’ But this is more than outweighed by exhortations to;

review their aims ...bearing in mind all the costs and impacts of their activity

or to integrate the views of;

those who experience the harmful consequences of production.

I believe that we should be moving beyond a policy approach that institutionalises presumed trade-offs between economic efficiency and social progress. We need to move from a consideration of shared responsibilities to the creation of shared value.

I am not talking about shared personal values. Nor is this about a redistribution approach, ‘sharing’ the value already created by companies. This is about expanding the total pool of economic and social value. I promoted this idea at this conference three years ago. It’s not original. Michael Porter and Mark Kramer proposed it as a new way to look at the relationship between business and society that does not treat corporate success and social welfare as a zero-sum game²⁰. Successful corporations need a healthy society, while education, healthcare and equal opportunity are essential to a productive workforce.

²⁰ Porter, M.E. and Kramer, M.R., 2006. Strategy & Society: The Link Between Competitive Advantage and Corporate Social Responsibility. Harvard Business Review, December 2006.

At the same time no social programme can rival the business sector when it comes creating the jobs, wealth and innovation that improve living standards. Choosing which social issues to address, they argue:

...is not whether a cause is worthy but whether it presents an opportunity to create shared value – that is a meaningful benefit for society that is also valuable to business. Efforts to find shared value in operating practices and in the social dimensions of competitive context have the potential not only to foster economic and social development but to change the way companies and society think about each other.

The concept rests on the premise that economic and social progress must be addressed using value principles. Value is defined as benefits relative to costs, not just benefits alone. Value creation is an idea that has long been recognised in business, where profit is revenues earned from customers minus the costs incurred. However, business have rarely approached social issues from a value perspective, but tended to treat them as peripheral matters.

The experience of the last three years makes this argument even more compelling. It has been suggested that the current crisis provides evidence that our economic model is broken and must be replaced. I disagree. The market continues to guarantee the most efficient allocation of resources. But I would accept that our recent experience highlights the dangers of viewing value creation narrowly. Business cannot afford to optimise short-term financial performance in a bubble while missing the most important customer needs and ignoring the broader influences that determine their long term success.

Governments and NGOs can enable and reinforce shared value or work against it. For example, regulation is necessary for well-functioning markets, something that became abundantly clear during the financial crisis. However, the approach to the way regulations are designed and implemented, determine whether they benefit society or work against it. Regulation that discourages shared value forces compliance with particular practices, rather than focusing on measurable social

improvement. It mandates a particular approach to meeting a standard, thereby blocking innovation and driving up business costs.

Appropriate regulations should set clear and measurable social goals, whether they involve energy use, health matters or safety. Where appropriate, they set prices for resources that reflect true cost. They set performance targets but do not prescribe the methods to achieve them. These are left to companies.

They define phase-in periods for meeting standards, which reflect investment or new-product cycle in industry. Phase-in periods give companies time to develop and introduce new products and processes in a way that is consistent with the economics of their business

They put in place universal measurement and performance-reporting systems, with government investing in infrastructure for collecting reliable benchmarking data. This encourages continual improvement. Finally they require efficient and timely reporting of results rather than expensive compliance processes.

There are signs of change. Efforts to minimise pollution were once thought to inevitably increase business costs and to only occur because of taxes and regulation. We now know that major improvements in environmental performance can be often be achieved with better technology that can even reduce business costs through better resource utilisation, process efficiency and quality. Heightened environmental awareness and advances in technology are also stimulating new approaches in areas such as utilisation of water, raw materials and packaging. Logistics systems are being redesigned to reduce shipping distances, streamline handling and improve vehicle routing.

All of these steps create shared value.

It is also important to remember the context within which we are developing policies of shared responsibilities. This is shaped by global issues over which Europe only has partial influence. These include the rise

of new economic powers in Asia and Latin America, higher capital and labour mobility around the world, climate change and the increased competition for natural resources.

Another lesson from our economic crisis is the degree to which Celtic Tiger Ireland became so insular on a range of important economic issues. We justified exorbitant asset prices and bloated salaries on a domestic economic mirage. We convinced ourselves that our circumstances were different to other economies which had experienced market bubbles and we built up a whole raft of public expenditures on unsustainable property related revenues. We completely lost sight of how we compared to most normal developed economies.

Ireland is one of the most open and globalised economies in the world. In order for us to rebuild our economy and get people back to work again we must continuously benchmark ourselves against other successful trading nations.

During the good years our public sector pay rates grew to be amongst the highest in the developed world, our idea of benchmarking was to compare public sector salaries to workers in our domestic economy not to similar positions in our trading partners. We grew our public expenditure at unprecedented rates and everything from education and health to social welfare rates benefited from the bubble economy. We decided we didn't like income taxes too much so through successive budgets we delivered the lowest effective income tax rates in the OECD and took about half of those at work out of the tax net completely. Some of these expenditure programmes represented catch up for years of under-investment but many of the economic policies taken during this period were entirely unsustainable. It is not a very popular fact but the reality is that every section of society benefited from the property fuelled tax revenues but of course some benefited much more than others did.

Ireland's economic future remains very bright and we retain capacity to deliver growth rates of about double that of the EU average. For this to happen, however, economic policy of the future can't be made in either

ignorance or defiance of trends in other countries. We need reasonable taxes to fund our public services; our public sector salaries must be comparable to those of our competitor countries; we must accept the necessity of local charges as part of an effective model of local government; our welfare and tax systems must interact in a manner which incentivises people to take up job offers.

The flaws of the Celtic Tiger economic model were evident to many observers who had spent time living and working internationally. They had seen it all before but yet the consensus in Ireland bought into the 'this time is different' theory. In seeking to rebuild our economy we must be much more open to the experiences of other successful economies.

We must also ensure that our response to the crisis remains focused on the need for Ireland to be flexible, innovative and competitive. Our future prosperity will depend on our ability to exploit global opportunities and to react quickly to changing market trends. Our crisis response cannot be isolationist and it would be counterproductive to pursue economic policies which run counter to developments in other developed countries. It would be futile for Ireland to act unilaterally on policy issues which may gain popular traction in a post crisis society. Our economy and society needs radical reform and change but this must be done in a manner which makes us more successful internationally and allows us to remain attractive for mobile international investment.

Society's needs are huge – health, improved nutrition, help for ageing, greater financial security, less environmental damage. Arguably they are the greatest unmet needs in the global economy. In advanced economies in particular, demand for products and services that meet social needs are rapidly growing. For example, food companies that traditionally concentrated on taste and quantity to drive more consumption are refocusing on the fundamental need for better nutrition. Some ICT companies are devising ways to help utilities to harness digital intelligence in order economise on power usage. Others are addressing the physical, cognitive and social consequences of ageing by using new technologies to help older people maintain their independence and to age in their own homes.

In these and many other ways, whole new avenues for innovation open up and shared value is created. Society's gains are even greater because businesses could be far more effective than governments and not-for-profit organisations at persuading customers to embrace products and services that create social benefits.

However, given the context of today's conference, it is also important to highlight that Porter and Kramer have extended the idea of shared value to not-for-profits and governments and they argue that this concept blurs the line between for-profit and not-for-profit organisations²¹. They also suggest that governments and NGOs will be most effective if they think in value terms – considering benefit relative to costs – and focus on the results achieved rather than the funds and effort expended.

They argue that the principle of shared value creation cuts across the traditional divide between the responsibilities of business and those of government or civil society. It doesn't matter what type of organisation creates the value. What matters is that benefits are delivered by those organisations or combinations of organisations that are best positioned to achieve the most impact for the least cost. Finding ways to boost productivity and innovation is equally valuable in the pursuit of commercial or social objectives.

The market economy is an unrivalled vehicle for meeting human needs, improving efficiency, creating jobs and building wealth. But a narrow conception of capitalism has prevented business from harnessing its full potential to meet society's broader challenges. We need a more sophisticated form of capitalism, one imbued with a social purpose. But it is completely unrealistic to suggest that a theoretical notion of shared social responsibilities is the most powerful force for addressing the pressing issues that society faces. This should come from a deeper understanding of competition and economic value creation.

²¹ Porter, M.E. and Kramer, M.R., 2010. Creating Shared Value: How to fix capitalism. Harvard Business Review, December 2010.